

BEFORE THE TENNESSEE REGULATORY AUTHORITY

AT NASHVILLE, TENNESSEE

OCTOBER 13, 1999

IN RE:

**UNITED TELEPHONE SOUTHEAST, INC.,
TARIFF TO REFLECT PROPOSED
CHANGES UNDER PRICE REGULATION PLAN**

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**DOCKET NO.
98-00626**

**ORDER REFLECTING THE DECISION REGARDING
THE 1998 PRICE REGULATION PLAN ADJUSTMENT
FOR UNITED TELEPHONE-SOUTHEAST, INC.**

This matter came before the Tennessee Regulatory Authority ("Authority") on the tariff filing of United Telephone Southeast, Inc. ("UTSE") to reflect proposed changes under its price regulation plan pursuant to Tenn. Code Ann. § 65-5-209. A hearing in this docket was held on May 13, 1999, and the Directors of the Authority subsequently deliberated the issues at the regularly scheduled Authority Conference held on August 10, 1999.

BACKGROUND

On September 15, 1998, UTSE filed its annual price cap adjustment pursuant to Tenn. Code Ann. § 65-5-209. Subsequently, on September 28, 1998, the Consumer Advocate Division, Office of the Attorney General ("Consumer Advocate") filed a "Complaint or Petition to Intervene" in this matter.¹ On October 16, 1998, UTSE amended its original filing to reflect the removal of a portion of the directory publishing fees from its price-cap

¹ Pursuant to Tenn. Code Ann. § 4-5-310(c), the Consumer Advocate was granted limited intervention, which precluded the Consumer Advocate from addressing any issues previously resolved by the Authority in Docket Nos. 96-01422, 96-01423 and 97-01438. See the Authority's Order entered on February 16, 1999.

calculations.

At a special Authority Conference held on November 24, 1998, the Consumer Advocate provided the Directors a copy of an agreement entered into with UTSE that would permit UTSE to place its tariffed rates into effect subject to refund. The Consumer Advocate assured the Authority that the agreement and UTSE's obligation to provide refunds, if necessary, protected the interests of Tennessee consumers. The Consumer Advocate also stated that the agreement provided additional protection because it contained provisions for the accrual of interest, the maintenance of customer records, the disposition of unclaimed funds and conditions of enforceability and termination.²

On November 20, 1998, Tri-Cities Airport Authority ("Tri-Cities") and Appalachian Northeast Tennessee Resource Conservation and Development Council ("Appalachian") filed Petitions to Intervene. The Authority attempted to deliberate on these petitions at regularly scheduled Authority Conferences held on December 15, 1998, January 19, 1999 and February 2, 1999. At each of the aforementioned Authority Conferences, the Directors provided an opportunity for Tri-Cities and Appalachian to discuss their respective petitions; however, after due notice, the petitioners either failed to appear before the Authority or otherwise failed to pursue their requests to intervene. BellSouth Telecommunication, Inc. ("BellSouth") filed a petition to intervene on January 29, 1999 and was granted intervention by the Authority at the February 2, 1999 Authority Conference.

At the January 19, 1999 Authority Conference, the Directors appointed the General Counsel or his designee to act as Pre-Hearing Officer in this matter for the purposes of acting on pre-hearing matters and presiding over any pre-hearing conferences. On February 2, 1999,

² The Authority accepted this agreement and permitted UTSE to place its rates into effect pursuant to an Order entered on March 23, 1999. A copy of the Authority's Order is attached to this Order as Attachment 1.

the Directors determined that the Pre-Hearing Officer should consider and resolve the pending petitions to intervene filed by Tri-Cities and Appalachian.

The Pre-Hearing Officer, Edward Phillips, acted on the pending petitions to intervene at a Pre-Hearing Conference held on March 9, 1999. In considering the petitions of Tri-Cities and Appalachian, the Pre-Hearing Officer noted that neither petitioner had a representative present to discuss the pending requests for intervention. Recognizing the continuing failure of Tri-Cities and Appalachian to attend scheduled conferences and/or failure to support their petitions, the Pre-Hearing Officer denied their petitions to intervene.³ At that Conference, the Pre-Hearing Officer also addressed the determination of the issues to be resolved and all matters pertaining to discovery. The Pre-Hearing Officer, with the agreement of the parties, established a schedule for conducting discovery and filing pre-filed testimony.⁴

HEARING ON THE MERITS

This matter came before the Directors of the Authority for a hearing on May 13, 1999.

At the Hearing the following appearances were entered:

United Telephone-Southeast, Inc. - **James Wright, Esquire**, 14111 Capital Boulevard, Wake Forest, North Carolina 27587-5900;

BellSouth Telecommunications, Inc. - **Guy Hicks, Esquire**, 333 Commerce Street, Suite 2102, Nashville, Tennessee 37201;

Consumer Advocate Division, Office of the Attorney General - **L. Vincent Williams, Esquire** and **Vance Broemel, Esquire**, 426 5th Avenue, N., 2nd Floor, Nashville, Tennessee 37243.

³ Subsequently, during a Special Authority Conference held on April 27, 1999, the Directors approved limited participation and not intervention for both Tri-Cities and Appalachian, which would permit both entities to monitor the proceeding and be served copies of the documents filed herein.

⁴ The decisions of the Pre-Hearing Officer were reflected in a Report and Recommendation filed on April 16, 1999 which was approved by the Authority at a Special Authority Conference held on April 27, 1999. The Authority's adoption of the Report and Recommendation, including the issues and procedural schedule, is reflected in its Order issued on April 30, 1999.

At the beginning of the Hearing, as a preliminary matter, the Directors considered UTSE's Motion to Strike and the Consumer Advocate's request to proffer evidence. In the pre-filed testimony of the Consumer Advocate's witness Terry Buckner, reference was made to 47 USC § 276(b)(1)(B) of the Telecommunications Act of 1996 as directing the FCC to "discontinue the intrastate and interstate carrier access charge payphone service elements and payments...and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenue..." Mr. Buckner stated that in CC Docket 96-128, the FCC ordered payphone subsidies to be removed and that as a result, UTSE reduced access charges by \$143,500 to remove its estimated payphone subsidy. Mr. Buckner concluded that the computations proposed by UTSE in this proceeding effectively restore this subsidy in violation of the FCC's Order.

The payphone subsidy issue addresses the effect on UTSE's price regulation filing wherein it removes the payphone "subsidy" through an access charge reduction in 1997. This issue was not included in the Consumer Advocate's list of issues filed prior to the Pre-Hearing Conference held on March 9, 1999. Although the Consumer Advocate raised the payphone subsidy issue at the Pre-Hearing Conference, the Consumer Advocate did not present the issue in a manner such that the Pre-Hearing Officer could determine its relevance to the issues in this proceeding. For this reason, the Pre-Hearing Officer did not include it as an issue for the hearing.

Because of its exclusion as an issue, UTSE filed a Motion to Strike that portion of Mr. Buckner's testimony that related to the payphone subsidy issue. The morning of the hearing, the Consumer Advocate attempted to introduce the written testimony of Mr. Archie Hickerson, which further related to the payphone subsidy; however, the Consumer Advocate

had not identified Mr. Hickerson as a witness prior to the morning of the hearing. The Consumer Advocate stated the he desired to introduce Mr. Hickerson's written testimony as a proffer of evidence to the Authority.

The Authority provided the parties the opportunity to present oral argument concerning UTSE's Motion to Strike and the Consumer Advocate's attempt to proffer Mr. Hickerson's testimony. UTSE argued that it would be prejudiced in the presentation of its case by the late introduction of Mr. Hickerson's testimony and the injection of the payphone subsidy issue into the proceeding. After much discussion, UTSE agreed to permit the introduction of Mr. Buckner's testimony on the payphone issue and to provide "spontaneous" rebuttal through the live testimony of Mr. Steve Parrott.⁵ In return, the Consumer Advocate agreed not to proffer Mr. Hickerson's testimony at any time during this case and presented the testimony of Mr. Buckner concerning the payphone subsidy issue.⁶ In addition, the Consumer Advocate was provided the opportunity during the hearing to cross-examine Mr. Parrott regarding the \$143,500 figure calculated by UTSE for the payphone subsidy docket. As a result of the parties' mutual resolution of these matters permitting the introduction of Mr. Buckner's testimony, the live rebuttal testimony of UTSE's witness, Mr. Parrot, relative to this issue, and the Consumer Advocate's withdrawal of its proffer, UTSE's Motion to Strike was rendered moot.

During the hearing on May 13, 1999 all parties to the proceeding were provided the opportunity to present live testimony and documentary evidence, conduct cross-examination

⁵ See May 13, 1999 Hearing Transcript at pp. 54-56.

⁶ See May 13, 1999 Hearing Transcript at p. 61. When specifically asked whether the Consumer Advocate would seek a proffer of evidence concerning the payphone issue, Mr. Williams, on behalf of the Consumer Advocate, answered that no such proffer would be re-submitted.

and submit rebuttal evidence. Mr. Steven Parrot testified on behalf of UTSE. The Consumer Advocate presented the live testimony of Mr. Terry Buckner. Parties filed Post-Hearing Briefs on June 28, 1999. The Consumer Advocate filed as part of its Post-Hearing Brief, a Motion to Continue the Hearing to Permit the Taking of Additional Discovery. On July 20, 1999, UTSE filed its response in opposition to the Motion. On July 21, 1999, BellSouth filed a letter supporting UTSE's opposition to the Consumer Advocate's request. In its Motion, the Consumer Advocate asserted that the Authority violated its "due process discovery" rights because the Consumer Advocate was not provided the opportunity to conduct discovery on the payphone subsidy issue. The Consumer Advocate asserted that it sought to preserve the issue through the presentation of its testimony. The Consumer Advocate further stated that the Authority "permitted UTSE to testify to unverified amounts of payphone costs."⁷ The record of the May 13th hearing does not support the Consumer Advocate's allegations.

The payphone subsidy issue was raised before the Authority through the Consumer Advocate's pre-filed testimony of Mr. Terry Buckner on April 30, 1999. Mr. Buckner's testimony contained references to the payphone subsidy issue after that issue had been excluded from consideration pursuant to the Pre-Hearing Officer's Recommendation of April 16, 1999. In his testimony, Mr. Buckner stated that UTSE had expressed an opinion in Docket No. 97-00409 as to the amount of the payphone subsidy equaling \$143,500. Mr. Buckner's testimony was introduced into evidence during the Hearing. Further, the Consumer Advocate had the opportunity to fully cross-examine UTSE witness Mr. Parrot during his rebuttal testimony, however elected not to do so. After the hearing was completed, the Consumer Advocate sought through its Motion to obtain discovery to produce additional

⁷ See the Post-Hearing Brief of the Consumer Advocate at p. 15.

evidence regarding the payphone subsidy issue as well as to continue the conduct of the hearing. After carefully reviewing the Motion and the record, the Directors determined that relative to UTSE's proposed payphone subsidy figure of \$143,500, the Consumer Advocate has sufficient opportunity to dispute that figure in Docket No. 97-00409. However, the Consumer Advocate requested a delay in the procedural schedule of that docket, until such time as the Universal Service proceeding (Docket No. 97-00888) is completed.

The parties to the Universal Service proceeding, including the Consumer Advocate, agreed that whatever rates are heretofore fixed by the Authority in Docket No. 97-00409 will be retroactive until April, 1997. As a result of that agreement, a true-up of the payphone subsidy will occur. Under these circumstances, it is inconsistent for the Consumer Advocate to assert that it should be permitted to determine the actual payphone subsidy figure in this case, when such figure will be forthcoming at the conclusion of Docket No. 97-00409. During the deliberations in the instant case on August 10, 1999, the Authority deducted the \$143,500 figure from UTSE's 1995 access revenues so that no subsidies associated with the de-regulated payphone operations would be absorbed by UTSE ratepayers on a going-forward basis.

The Authority's action in this case obviates a part of the Consumer Advocate's concerns. Any of the Consumer Advocate's concerns that remain regarding the payphone subsidy issues are still to be resolved by the Authority in Docket No. 97-00409. The additional consideration of the payphone subsidy issue should provide the Consumer Advocate with the opportunity to refute the \$143,500 figure in the context of Docket No. 97-00409, and if any deficiency is found to exist, the Authority will adjust UTSE's 1995 access revenues and future rates accordingly.

FINDINGS OF FACT AND CONCLUSIONS OF LAW

Based upon the evidentiary record in this case, the Directors of the Authority deliberated on the following four (4) issues at the August 10, 1999 Conference:

Issue 1: **Does the application of the methodology as applied to UTSE's proposed 1998 aggregate revenue cap adjustment result in an increase that is not permitted under Tenn. Code Ann. § 65-5-209?**

This issue centers on the requirements of Tenn. Code Ann. § 65-5-209 and an earlier stipulation between the parties in this proceeding regarding the appropriate methodology for implementing the relevant sections of this statute. This stipulation was entered into by the parties in 1996 as part of Docket No. 96-01423, *United Telephone-Southeast, Inc. Tariff No. 96-201 to Reflect Annual Price Cap Adjustment* and subsequently applied to UTSE's 1997 price regulation filing in Docket No. 97-01438.⁸ In both of those cases, the Consumer Advocate appealed the TRA's decision, but did not challenge the legality of the stipulated methodology accepted by the TRA.⁹ There is no issue concerning UTSE's application of or calculations under the stipulated methodology in this case.¹⁰

Position of the Parties

The issue presented by the parties is whether the price increase requested by UTSE exceeds the amount allowed by law. The Consumer Advocate claims that UTSE's calculation in this case violates Tenn. Code Ann. § 65-5-209(e) by permitting a price adjustment that

⁸ A copy of the stipulation entered into by the parties is attached to this Order as Attachment 2.

⁹ The stipulated methodology calculates two (2) indices: the Price Regulation Index ("PRI") and the Service Price Index ("SPI"). The PRI is an adjusted inflation index based on the Chain-Weighted Gross Domestic Product-Price Index ("GDP-PI") since the inception of price regulation for UTSE in 1995. The 1998 PRI calculated by UTSE is 100.2940. The SPI is the ratio of UTSE revenues calculated using UTSE's proposed rates to those revenues calculated using the rates in effect on June 5, 1995.

¹⁰ See Post-Hearing Brief of UTSE at p. 6; and the Post-Hearing Brief of the Consumer Advocate at p. 4.

exceeds the cap on the “maximum annual adjustment.” The Consumer Advocate asserts that UTSE’s computation violates the above statute because it yields a cumulative adjustment that surpasses the allowable adjustment permitted for a single year.

The Consumer Advocate contends that UTSE’s proposed rates increase its aggregate revenues by 4.72%, which exceeds the “maximum annual increase” of negative 0.8% under Tenn. Code Ann. § 65-5-209(e).¹¹ That is, UTSE’s rates should be **reduced** such that its revenues decline by 0.8%. This is the change in the GDP-PI over the preceding year as adjusted by Tenn. Code Ann. § 65-5-209(e), referred to as the **annual** adjustment.¹² The stipulated methodology determines a maximum **cumulative** increase allowed over a period of years, but the Consumer Advocate contends that Tenn. Code Ann. § 65-5-209(e) also limits the annual increase allowed in any one year.¹³ If UTSE actually took the maximum increase allowed in each year, the two limits would result in the identical outcomes.¹⁴

UTSE disagrees with this position and asserts that the stipulated methodology is applied by calculating two indices. The first index is the Price Regulation Index (the “PRI”) which is calculated from the inception of UTSE’s price regulation plan. The second index,

¹¹ See Pre-filed Direct Testimony of Mr. Buckner at p. 6. The Consumer Advocate’s Post-Hearing Brief at p. 5 erroneously indicates a **positive** 0.8% as the maximum allowed increase. Some confusion exists in the record over the calculation of the annual increase as proposed by the Consumer Advocate. Mr. Williams’ questioning of Mr. Parrott suggests either: 1) comparing the change in revenues between the proposed July 1998 rates and the actual June or July 1997 rates; or 2) comparing the June 1998 rates with the proposed July 1998 rates (May 13, 1999 Hearing Transcript at pp. 175-190). In response to questioning by Director Greer, Mr. Buckner stated that his calculations compare revenues at June 1998 rates to revenues at proposed July 1998 rates (May 13, 1999 Hearing Transcript at pp. 228-32). Mr. Parrott stated that this is the same as comparing the revenues under the change in rates from 1997 to 1998 only if UTSE made no rate adjustments during that period, but did not state whether such rate changes had occurred. (May 13, 1999 Hearing Transcript at pp. 183-4). Further, Attachment C to Mr. Buckner’s Pre-filed Direct Testimony compares hypothetical price changes from the previous year’s rates to the current year’s proposed rates, but assumes that the previous year’s rates are unchanged up to that time.

¹² See the Post-Hearing Brief of the Consumer Advocate at p. 6.

¹³ See Pre-filed Direct Testimony of Mr. Buckner at pp. 3-4.

¹⁴ See the Post-Hearing Brief of the Consumer Advocate at p. 6.

the Service Price Index (the “SPI”) is calculated as a ratio of UTSE’s proposed rates to UTSE’s revenues calculated using the rates in effect on June 5, 1995. UTSE asserts that, to the extent that the SPI does not exceed the PRI which represents the cap on UTSE’s aggregate revenues, the company is in compliance with Tenn. Code Ann. § 65-5-209. UTSE denies any legal prohibition on a maximum annual increase, as long as its adjustments comport with the stipulated methodology; which UTSE believes comports with § 65-5-209. BellSouth supports UTSE’s position.

UTSE witness Mr. Parrott states that the application of the “annual” versus “cumulative” methods as claimed by the Consumer Advocate results in a situation of “use or lose it.”¹⁵ That is, under the approach advocated by the Consumer Advocate, a price-regulated company must increase rates at every opportunity, staying continually at the cap, so that it will not lose the opportunity for a rate increase. UTSE contends that this is not in the public interest as it creates a situation in which prices will or could increase much sooner than would otherwise occur under UTSE’s application of the methodology.

BellSouth asserts that § 65-5-209(e) permits UTSE to charge rates, at any time, that generate aggregate revenues equal to those that would have been generated if UTSE had taken advantage of the maximum rates permitted in every single year since entering price regulation. UTSE may also defer rate increases to accumulate “headroom.” In fact, the General Assembly’s specific prohibition of price increases for basic residential service that exceed the increase in inflation (the percentage change in GDP-PI) from the previous year implies that such increases for other services could occur. The argument that such a “year over year” limitation applies only to basic residential rates suggests that there is no such

¹⁵ See Pre-filed Rebuttal Testimony of Mr. Parrott at p. 7.

limitation on other rates, contradicting the Consumer Advocate's argument for a maximum annual increase.¹⁶ Moreover, BellSouth claims that there is no such "year-over-year" limitation in the stipulated methodology as the Consumer Advocate suggests.¹⁷ Finally, BellSouth also asserts that the imposition of such a restriction would harm consumers by forcing price-regulated companies to seek maximum price increases as soon as permitted under the price-regulation statutes.¹⁸

Findings

The resolution of this issue hinges on the interpretation of Tenn. Code Ann. § 65-5-209(e), which states in pertinent part as follows:

A price regulation plan shall maintain affordable basic and non-basic rates by **permitting a maximum annual adjustment** that is capped at the lesser of one half (1/2) the percentage change in inflation for the United States using the gross domestic product-price index (GDP-PI) from the preceding year as the measure of inflation, or the GDP-PI from the preceding year minus two (2) percentage points. An incumbent local exchange telephone company **may adjust its rates** for basic local exchange telephone services or non-basic services only so long as its aggregate revenues for such basic local exchange telephone services or non-basic services generated by such changes **do not exceed the aggregate revenues generated by the maximum rates permitted** by the price regulation plan. (Emphasis supplied).

The Consumer Advocate's argument places an emphasis on the first sentence, specifically on the language pertaining to an "annual adjustment." The argument of UTSE and BellSouth places an emphasis on the second sentence, specifically the language that makes any adjustment optional ("may adjust"), with such adjustments not exceeding the maximum rates permitted.

¹⁶ See Post-Hearing Brief of BellSouth at pp. 3-4.

¹⁷ See Post-Hearing Brief of BellSouth at pp. 6-7.

¹⁸ See Post-Hearing Brief of BellSouth at p. 8; and May 13, 1999 Hearing Transcript at p. 192.

The language of Tenn. Code Ann. § 65-5-209(e) refers to a “maximum annual adjustment” but does not set forth the manner in which this adjustment is to be applied. Further, the language of the statute indicates that a company’s actual rates may deviate from the “maximum rates permitted” by law, but is silent as to how this might occur. The conflicting positions of the parties reflect this lack of direction in the statute. The Consumer Advocate asserts that the “maximum annual adjustment” applies to a company’s actual rates, negating any accumulation of “headroom” from one year to the next. UTSE and BellSouth argue that the “maximum annual adjustment” applies to the “maximum rates permitted,” allowing the accumulation of “headroom” and the possibility that rates could increase in a single year by more than the capped “maximum annual adjustment” described under Tenn. Code Ann. § 65-5-209(e).

Sub-section (e) is clear in that there must be some method for determining “the aggregate revenues generated by the maximum rates permitted by the price regulation plan.”¹⁹ An additional requirement of Tenn. Code Ann. § 65-5-209(e) is that *the price regulation plan* “maintain affordable Basic and Non-Basic rates by permitting a maximum annual adjustment that is capped” by the inflation formula described therein. Under this statutory scheme, the Authority is empowered to approve price regulation plans pursuant to the guidelines announced under Tenn. Code Ann. § 65-5-209. The Authority is required to determine the proper procedures by which a price-regulated company must abide so that the appropriate annual adjustment and rate increases are implemented vis-à-vis the company’s price regulation plan. The stipulated methodology as applied by UTSE defines a means of

¹⁹ See also sub-section (b) (a company “...shall charge and collect only such rates that are less than or equal to the maximum permitted by this section...”) and (h) (“...Companies subject to price regulation may set rates for Non-Basic Services as the company deems appropriate, subject to the limitations set forth in subsections (e) and (g)...”).

establishing the aggregate revenues, the maximum rates, and the application of the maximum annual adjustment as required by Tenn. Code Ann. § 65-5-209. The Consumer Advocate acknowledges the critical importance of the parts of the stipulation except for the results of the “maximum annual adjustment.”²⁰ As UTSE and BellSouth assert, UTSE’s approach better serves the public interest because price increases are more likely to be delayed under this application of the methodology. This point was not challenged by the Consumer Advocate.²¹

The Authority finds that the stipulated methodology as applied by UTSE in this case complies with Tenn. Code Ann. § 65-5-209. No evidence has been presented to demonstrate that Tenn. Code Ann. § 65-5-209 requires forfeiture for any given annual period in which a company elects not to seek a rate increase. A finding contrary to this would suggest that price-regulated companies must raise consumers’ rates each year, or otherwise forever lose the opportunity to seek such an increase, which obviously is contrary to the public interest.²²

Issue 2: **Should the earnings of UTSE’s directory affiliate be included in the aggregate revenue cap?**

Positions of Parties

The Consumer Advocate asserts that the aggregate revenue cap adjustment is deficient because it does not include the imputation of earnings from UTSE’s Yellow Page affiliate as

²⁰ In fact, the Consumer Advocate acknowledges that “...the stipulation is absolutely critical for determining the “aggregate revenues” referred to in Tenn. Code Ann. § 65-5-209(e),” and that it takes the guess-work out of determining service volumes, especially the stimulation/destimulation in response to price changes (Post-Hearing Brief of the Consumer Advocate at p. 7-8).

²¹ See Post-Hearing Briefs of UTSE at p. 8; BellSouth at p. 8, and Consumer Advocate at pp. 1-8.

²² This finding only applies to the aggregate revenue cap for the non-basic category of services. The aggregate revenue cap for the basic category of services, which are frozen for four years by statute, would likely be treated differently.

required by the Tennessee Public Service Commission in 1995 when UTSE's initial rates were approved.²³ The Consumer Advocate also contends that UTSE's position to remove the directory base publishing fees from the aggregate revenue cap base year is incorrect. The Consumer Advocate argues that the Authority should require UTSE to revise its filing to include Yellow Page revenues in both the base period and proposed aggregate revenues.²⁴

UTSE counters that the imputation of Yellow Page earnings is a rate of return calculation and is not a proper adjustment under the aggregate revenue cap methodology. UTSE contends that it has not eliminated the Yellow Page earnings imputation from its rates as the Consumer Advocate alleges. Instead, UTSE argues that its consumers continue to receive the benefit from the effects of the imputed Yellow Page revenues today.²⁵

Findings

It is inconsistent with Tenn. Code Ann. § 65-5-209 to include Yellow Page earnings in the aggregate revenue cap. The imputation of Yellow Page earnings is a rate of return calculation utilized in 1995 in establishing UTSE's initial rates under price regulation. However, subsequent to the establishment of the initial revenue cap, a company's earnings are no longer considered. *See* Tenn. Code Ann. § 65-5-209(e), which in pertinent part states as follows:

An incumbent local exchange telephone company may adjust its rates for basic local exchange telephone services or non-basic services only so long as its aggregate **revenues** for basic local exchange telephone services or non-basic services generated by such changes do not exceed the aggregate **revenues** generated by the maximum rates permitted by the price regulation plan. (Emphasis supplied)

²³ *See* Pre-filed Direct Testimony of Mr. Buckner at p. 5; *see also*, Post-Hearing Brief of the Consumer Advocate at p. 8.

²⁴ *See* Post-Hearing Brief of the Consumer Advocate at pp. 14–15.

²⁵ *See* Pre-filed Rebuttal Testimony of Mr. Parrott at pp. 2–3.

The statute requires that the aggregate revenue cap is to include revenues, not earnings, and therefore the Consumer Advocate's proposed adjustment is rejected.

Issue 3: Should rate reductions to affiliated companies for directory listings be included in the aggregate revenue cap?

Positions of the Parties

UTSE's filing reflects a \$135,310 decline in directory revenues resulting from a decrease in the charges by UTSE to Sprint Corporation's wholly owned directory affiliate, Sprint Publishing and Advertising, for directory listings.²⁶ UTSE argues that the directory listing rate has been reduced to all companies, not just to its affiliated publisher.²⁷ The Company proposes to recover the lost revenues from this rate reduction from its consumers, stating that the rate reduction is in accordance with the approved price methodology.

As stated previously, the Consumer Advocate contends that all directory operations (revenues, expenses and profit) should be included in the aggregate revenue cap. Therefore, inclusive in this position is the premise that UTSE should not be permitted to offset an affiliate reduction with a rate increase to other non-affiliated services.

Findings

In essence, UTSE reduced charges to its affiliate and now proposes to recover the lost revenues from its end users. UTSE's inclusion of a \$135,310 reduction in charges to its affiliated entity, Sprint Publishing and Advertising, along with its associated proposal to recover this reduction through increased rates to consumers is not in the public interest, is

²⁶ The rate decreased from \$0.65 per listing to \$0.04 per listing. The base year (1995) includes \$194,000 in directory listing revenue while the current year includes \$58,000. UTSE and Sprint Publishing and Advertising are both wholly owned subsidiaries of Sprint Corporation.

²⁷ See Post-Hearing Brief of UTSE at p. 13.

inconsistent with the stated intent of the General Assembly and contradicts the testimony of UTSE witness Parrott.

It is obvious that the General Assembly did not intend for the Authority to allow such adjustments in the regulatory mechanism . In addition to establishing a price floor to prevent anti-competitive activity, Tenn. Code Ann. §65-5-208(c) states in part:

....The Authority shall, as appropriate, also adopt other rules or issue orders to prohibit cross-subsidization, preferences to competitive services **or affiliated entities**, predatory pricing, price squeezing, price discrimination, tying arrangements or other anti-competitive practices. (Emphasis added)

Offsetting reductions to affiliates by increasing rates to non-affiliates clearly gives preference to an “affiliated entity.” Given such a direction by the statute, the Authority finds that it is not in the public interest or consistent with Tenn. Code Ann. § 65-5-208 to allow UTSE to recover lost affiliate charges from its customers. By its own admission, UTSE indicates that it is improper to include reductions to affiliates in the aggregate revenue cap.²⁸ UTSE witness Parrott, in explaining why the company decided to amend its filing to remove affiliate base publishing fees from the aggregate revenue cap calculation, stated:

The only reason that we amended the filing was, in looking at that one particular item, which was exclusively between us and an affiliate directory publishing company, did not reflect and would never affect any other publishing company. What we decided was that it was improper to extract from our customers the fact that revenue that we were receiving from the affiliate under the old agreement now we were no longer receiving. We did not believe it was appropriate or in the public interest to extract that from our customers, since it related solely to a contract and services rendered between us and that affiliate.²⁹

²⁸ Transcript, Page 134.

²⁹ Transcript, Page 134.

Although UTSE witness Parrott is referring to base publishing fees paid by an affiliate for publishing an exclusive directory for UTSE, Parrott's reasoning may logically be applied to other affiliate transactions such as directory listings.³⁰ Thus, the Authority concurs with Mr. Parrott's position that it is not in the public interest to recover from its customers, reduced charges to affiliate companies. Therefore, to ensure that the company does not recover from its ratepayers the reductions made to the affiliated publishing company, UTSE is directed to remove the directory listing revenues received from its affiliate publishing company from the base year and current year calculations. This would result in the removal from the base year revenues in the amount of \$144,183 and the current year's revenue calculations in the amount of \$8,873.³¹

Issue 4: How should the payphone subsidy previously removed be accounted for in calculating UTSE's annual aggregate revenue cap calculation?

Positions of the Parties

In April of 1997, acting in Docket 97-00409, the Directors of the Authority ordered UTSE to reduce its intrastate access charges by \$143,500; a figure that represents UTSE's estimated payphone subsidy. UTSE's filing includes current access charge rates for purposes of calculating the aggregate revenue cap. Included in these rates is the adjustment to reflect the removal of the payphone subsidy.

The Consumer Advocate did not challenge the fact that UTSE has reduced its access charges by \$143,500 so as to remove the subsidy from payphone operations that had

³⁰ While UTSE contends that the directory listing rate has been reduced to all publishing companies (UTSE Post Hearing Brief, Page 13), the record shows that 99.55% of the directory listings are purchased by Sprint Advertising and Publishing.

³¹ The Authority finds that it is appropriate to include non-affiliate portion of the directory listing reduction in the calculation of the aggregate revenue cap.

previously flowed to other services. The Consumer Advocate, however, contends that if the base rates as proposed by UTSE were used in calculating the SPI, the subsidy previously removed would, in effect, be restored. The Consumer Advocate asserted that the base year revenues should be adjusted to reflect the removal of the payphone subsidy to ensure that the subsidy is not recovered through the aggregate revenue cap. The Consumer Advocate also states that UTSE's proposal would violate the FCC's payphone Orders by permitting the subsidy to be recovered.³²

UTSE contends it has complied with 47 USC § 276(b)(1)(B) and related FCC orders entered in CC Docket 96-128 by its reduction of intrastate switched access rates (originating Carrier Common Line Charge) by the amount of the payphone subsidy estimated at that time. As a result of this position, UTSE failed to propose an alteration to its aggregate revenue cap plan concerning payphone subsidies. UTSE and BellSouth both contend that adopting the Consumer Advocate's argument to remove the payphone subsidy would require the recalculation of base year revenues and rates. The two parties argue that Tenn. Code Ann. § 65-5-209 does not support such a recalculation of base year rates.³³ Further, UTSE and BellSouth state that nothing in Section 276(b)(1)(B) or any FCC order preempts Tennessee law regarding intrastate price regulation. In summary, UTSE and BellSouth contend that there is no legal basis for allowing the recalculation of UTSE's initial rates.³⁴

Findings

This issue centers on how the aggregate revenue cap methodology and UTSE's rates

³² See Pre-filed Direct Testimony of Mr. Buckner at p. 5.

³³ See Post-Hearing Brief of UTSE at pp. 17–18, and Post-Hearing Brief of BellSouth at p 9.

³⁴ See Post-Hearing Brief of UTSE at p. 17.

should continue to reflect the removal of the payphone subsidy. UTSE would recover the previously removed subsidy through its aggregate revenue cap filing if it did not account for the removal of the subsidy from the revenue cap, as required by the FCC's mandate that such rates be removed. Therefore, given the requirements established by both 47 USC § 276(b)(1)(B) and the FCC, the Authority agrees with the Consumer Advocate that the base year's revenues should be adjusted to ensure that the payphone subsidy is not restored in UTSE's rates. Accordingly, the base year (1995) revenues should be restated to reflect the access rate reduction made for the removal of the payphone subsidy.³⁵

The contention by BellSouth and UTSE that Tennessee law does not support adjusting the revenue cap to remove the payphone subsidy is without merit. UTSE's treatment of the payphone subsidy is inconsistent with both state and federal statutes. Section 276(b)(1)(B) of the Federal Telecommunications Act directs the FCC to "discontinue the intrastate and interstate carrier access charge payphone service elements and payments... and all intrastate and interstate payphone subsidies from basic exchange and exchange access revenue..." It is not logical to conclude that Congress would require the removal of the payphone subsidy, only to permit states to turn around and add the subsidy back by increasing rates to consumers as UTSE proposes. Any such action would clearly undermine the directive set forth by Congress and the FCC and would likely be preempted by the FCC as permitted in Section 276(c) of the Federal Telecommunications Act.

Furthermore, state law addresses cross-subsidies such as the payphone subsidy. As noted previously, Tenn. Code Ann. § 65-5-208(c) provides in part:

³⁵ The final determination for the amount of payphone subsidies to be removed will be decided in TRA Docket No. 97-00409, *Tariff Filings Regarding the Reclassification of Pay Telephone Service As Required By FCC Docket 96-128*. If the amount of the subsidy is revised, the aggregate revenue cap should be amended accordingly.

The Authority shall, as appropriate, also adopt other rules or issue orders to **prohibit cross-subsidization**, preferences to competitive services or affiliated entities, predatory pricing, price squeezing, price discrimination, tying arrangements or other anti-competitive practices. (Emphasis supplied).

The reason that the payphone subsidy was removed and rates were reduced was to prohibit the cross-subsidization between a service deemed competitive by the FCC and the other services of the incumbent. Consistent with Tennessee law, the Authority must prevent the reinstatement of this cross-subsidization.

Therefore, consistent with state and federal statutes, UTSE is ordered to remove from the aggregate revenue cap the access charge reductions ordered by the Authority in 1997 to eliminate the payphone subsidy.³⁶ By including the access rates at current levels in the calculation of the aggregate revenue cap and not adjusting for the payphone subsidy, in effect UTSE is adding the payphone subsidy back into UTSE's rates, thus violating FCC Docket 96-128 and Section 276(a) of the Federal Telecommunications Act.^{37/38}

³⁶ By spinning off its payphone operations from the incumbent telephone company and removing any subsidy in existing rates by reducing access charges, Sprint Corporation's payphone rates were deregulated in 1997 consistent with FCC Docket 96-128.

³⁷ Although UTSE was ordered to reduce rates to eliminate the payphone subsidy, Sprint's payphone affiliate subsequently increased the price of a payphone call to \$.35 in 1997.

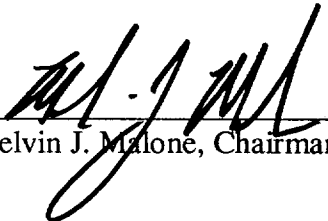
³⁸ Director Greer dissented with the majority on this issue stating that: "I believe that not only did the Consumer Advocate not prove his point, but he also left me to wonder what his point was. Mr. Buckner's testimony was not clear to me. Additionally, the Consumer Advocate had the opportunity at the hearing to cross-examine Mr. Parrott regarding the 143,500-dollar figure calculated by UTSE for the payphone subsidy docket, but failed to rebut or refute this figure. Further, the FCC may have directed the removal of the pay phone subsidy, but I do not find where the FCC specifically prohibited the subsequent recovery of this revenue. Therefore, I move that UTSE be allowed to include the pay phone subsidy in its price cap calculation."

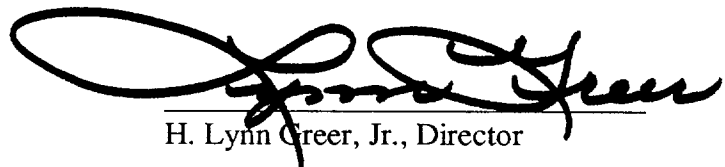
Based upon the foregoing findings of fact and conclusions of law,

IT IS THEREFORE ORDERED THAT:

1. The “Motion to Continue Hearing and Permit the Taking of Additional Discovery” filed by the Consumer Advocate Division is denied.
2. Tariff No. 98-00626 filed by United Telephone-Southeast is hereby denied.
3. The Stipulated Methodology as applied by United Telephone-Southeast in this case complies with Tenn. Code Ann. § 65-5-209, and is therefore adopted.
4. Based on the finding that it is inconsistent with Tenn. Code Ann. § 65-5-209 to include earnings of United Telephone-Southeast Inc.’s directory affiliate in the aggregate revenue cap, United Telephone-Southeast Inc. is directed to amend its filing to reflect the removal of directory listing revenues received from its affiliate publishing company from the base year and from the current year’s calculation of the aggregate revenue cap.
5. United Telephone-Southeast, Inc. shall amend its filing to restate base year access revenues to reflect the removal of the payphone subsidy ordered by the Authority in Docket No. 97-00409.
6. United Telephone-Southeast, Inc. shall amend its filing no later than August 24, 1999. The amended filing should include a proposal for adjusting rates on a going-forward basis consistent with this Order and with a proposal for customer refunds consistent with the approved stipulation between UTSE and the Consumer Advocate.
7. Any party aggrieved by the Tennessee Regulatory Authority’s decision in this matter may file a Petition for Reconsideration with the Authority within ten (10) days of the date of this Order.

8. Any party aggrieved with the Tennessee Regulatory Authority's decision in this matter has the right of judicial review by filing a Petition for Review in the Tennessee Court of Appeals, Middle Section, within sixty (60) days from and after the date of this Order.


Melvin J. Malone, Chairman


H. Lynn Greer, Jr., Director


Sara Kyle, Director

ATTEST:


K. David Waddell, Executive Secretary

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

IN RE:	MARCH 23, 1999)	
)	
UNITED TELEPHONE SOUTHEAST, INC. TARIFF)	DOCKET NO.
TO REFLECT PROPOSED CHANGES UNDER)	98-00626
PRICE REGULATION PLAN)	

**ORDER PERMITTING UNITED TELEPHONE SOUTHEAST, INC. TO PLACE
RATES INTO EFFECT UNDER BOND AND PURSUANT TO THE TERMS OF
AN AGREEMENT REACHED WITH THE CONSUMER ADVOCATE PENDING
FINAL DISPOSITION OF THE CONTESTED CASE PROCEEDING BY THE
TENNESSEE REGULATORY AUTHORITY**

This matter came before the Tennessee Regulatory Authority ("Authority") on the above-docketed tariff filing of United Telephone Southeast, Inc. ("UTSE") to reflect proposed changes under its price regulation plan pursuant to Tenn. Code Ann. § 65-5-209. The Authority considered matters related to this tariff filing at a Special Authority Conference held on November 24, 1998.¹ At that Conference, the Directors of the Authority considered UTSE's request that it be permitted to place its proposed tariff into effect.

UTSE filed its original tariff on September 15, 1998, with a proposed effective date of October 15, 1998, as a part of its annual price cap filing. At the October 6, 1998, Authority Conference, the original tariff was suspended for thirty (30) days from its proposed effective date. UTSE filed a revised tariff on October 16, 1998, proposing a

¹ This Special Conference was scheduled with the agreement of the parties during a regularly scheduled Authority Conference held on November 17, 1998.

ATTACHMENT

new effective date of November 18, 1998. The Consumer Advocate Division, Office of the Attorney General ("Consumer Advocate") filed a Complaint or Petition to Intervene on September 29, 1998. At the November 3, 1998, Authority Conference, the Consumer Advocate requested that its Petition be considered at the Authority's November 17th Conference. UTSE's revised tariff was suspended by the Authority until the November 17th Conference, with the suspension ending just prior to the revised tariff's proposed effective date of November 18, 1998.

At the November 17th Conference, the Consumer Advocate advised the Directors that he would agree to permit UTSE to place the tariff into effect under bond. UTSE agreed to accept the Consumer Advocate's proposal.² As a result of this agreement, the Authority directed the Consumer Advocate and UTSE to submit to the Authority their agreement in writing that would permit UTSE to place its rates into effect under bond.

At the November 24, 1998, Special Authority Conference, the Consumer Advocate provided to each Director a copy of the "Agreement regarding Actions to be Taken in the Event a Refund of Rates is Required" ("Agreement") entered into between UTSE and the Consumer Advocate. Under the Agreement, UTSE would place its tarified rates into effect. The agreement outlined actions to be taken by UTSE in the event a refund was necessitated as a result of the disposition of the contested case. The Consumer Advocate advised the Authority that the interests of Tennessee consumers were appropriately protected through the Agreement and UTSE's obligation thereunder to

² At the November 17, 1998, Conference, Chairman Malone suggested to the Consumer Advocate and UTSE that if they entered into an agreement to place the rates into effect under bond, that such agreement be filed with the Authority for approval, and that the parties to the agreement provide to the Authority the legal support for approving the same.

provide for refunds should the Authority's decision lead to such a result. To ensure that consumers are not harmed, the Agreement contains provisions for interest, the maintenance of customer records, the disposition of unclaimed funds and conditions of enforceability and termination.

During a discussion regarding the necessity for Authority review and approval of the Agreement, the Consumer Advocate represented to the Authority that the Agreement did not require formal approval by the Authority. Thereafter, a majority of the Directors determined that there was no need for the Authority to approve the Agreement and determined further that, based on the statements of the Consumer Advocate, the interests of consumers were protected by the requirements in the Agreement. Based on UTSE's agreement to assume the risk of placing rates into effect with the possibility that it may have to make refunds to Tennessee Consumers, a majority of Directors voted to permit UTSE to place its rates into effect under bond and in accordance with the terms of the Agreement.³ The rates that UTSE may place into effect are those provided for in the revised tariff filing of October 16, 1998.

³ It must be noted Director Greer's prevailing motion on November 24, explicitly reflected his intention that the rates go into effect under bond, when he made the following statement:

I think the customers rights are protected. Therefore, I'm willing to let the rates go into effect under this bond agreement that the two parties have come up with. November 24, 1998, Special Authority Conference Transcript at 13.

The parties did not object to or comment on Director Greer's statement. However, while the agreement submitted by the parties on the morning of November 24, 1998, correctly reflects the offer made by the Consumer Advocate at the November 17th Conference which originally required the rates to go into effect under bond, the agreement as submitted contains a provision that the rates will go into effect in lieu of bond so long as UTSE agrees to refund any excess amount over the actual approved rate increase permitted by the Authority at the conclusion of this proceeding. This agreement is not in accord with the understanding of the majority of the Directors, nor the offer made by the Consumer Advocate. See November 17, 1998, Authority Conference Transcript at 70.

IT IS THEREFORE ORDERED THAT:

1. UTSE's proposed revised tariff is effective as of November 18, 1998, with the proposed rates contained therein becoming effective on that date under bond and subject to the terms and conditions that are consistent with this decision and are set forth in an Agreement between UTSE and the Consumer Advocate.

2. Any party aggrieved by the Authority's decision in this matter may file a Petition for Reconsideration with the Authority within ten (10) days after the date of this order.

CHAIRMAN



DIRECTOR

ATTEST:



DIRECTOR



EXECUTIVE SECRETARY

**** Chairman Malone did not join the action of the majority.

BEFORE THE TENNESSEE REGULATORY AUTHORITY

NASHVILLE, TENNESSEE

**IN RE: UNITED TELEPHONE-SOUTHEAST, INC.'S TARIFF TO
REFLECT PROPOSED CHANGES UNDER PRICE REGULATION
PLAN**

Docket No. 98-00626

SEPARATE OPINION OF CHAIRMAN MELVIN MALONE

While I respect the opinion of the majority, I am compelled to write separately because the parties did not file the agreement at issue in a sufficiently timely manner in order to provide the Tennessee Regulatory Authority (the "Authority") with a reasonable opportunity to review and consider the same.

At the November 17, 1998, Authority Conference, the Consumer Advocate offered to permit United Telephone-Southeast Inc.'s ("UTSE") proposed rate increases under its price regulation plan to go into effect under bond pending approval of the Authority and UTSE accepted the Consumer Advocate's offer. See November 17, 1998, Authority Conference Transcript at 70 and 80. The parties were directed to submit an agreement in writing for consideration and approval by the Directors. It was my understanding, based upon comments made at the November 17, 1998, Authority Conference, that the parties would provide legal support for such an agreement.

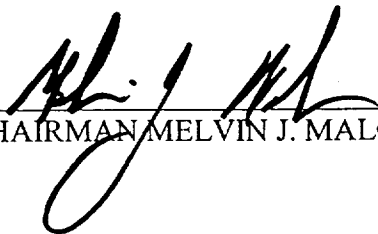
On the morning of November 24, 1998, at a Special Authority Conference, the parties submitted, without any legal authority whatsoever, a document styled "Agreement Regarding

Actions to be Taken in the Event a Refund of Rates is Required" (hereinafter the "Agreement"). The Agreement had not been previously filed with the Authority.¹

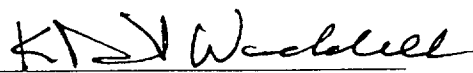
At the Special Conference, I stated that I was not opposed, to the extent permitted by law, to either the rates going into effect under bond subject to the approval of the Authority or the rates going into effect by some agreement of the parties. See id. at 14. What concerned me then, and no less concerns me now, is that at the time the majority acted on the Agreement, the Authority had not been afforded, by the parties, the opportunity to adequately review and consider both the policy and legal implications of the Agreement. See id. As is my custom, I declined to substantively comment upon or take official action on a filing that the agency had not been provided an opportunity to review.

For the foregoing reasons, it was my opinion at the November 24, 1998, Authority Conference, and remains my opinion today, that the Authority should have deferred consideration of the Agreement until a later time. Hence, I did not, and do not here, join in the position of the majority.

Respectfully submitted,


CHAIRMAN MELVIN J. MALONE

ATTEST:


Executive Secretary

¹ Although the parties were well aware that the Agreement would be presented to the Authority on November 24, 1998, it was not filed with the Authority until November 24, 1998.



Sprint
Mid Atlantic Telecom

Carolina Telephone
Centel-North Carolina
Centel-Virginia
United Telephone-Southeast

James B. Wright
Senior Attorney

January 27, 1997

Chairman Lynn Greer
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505

RE: Docket No. 96-01423

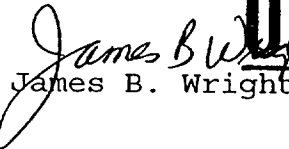
Dear Chairman Greer:

On behalf of all the parties of record in the above case, enclosed is a written Stipulation which reflects the parties' agreement regarding methodology applicable to the above case.

This Stipulation is being formally filed of record in accordance with the procedural schedule set forth in the parties' Joint Motion dated January 16, 1997.

Please contact me if you have any questions.

Very truly yours,


James B. Wright

JBW:er

CC: David Waddell (with 10 enclosures)
Dianne Neal (with enclosure)
Counsel of Record (with enclosure)
C. Steve Parrott (with enclosure)

OFFICIAL FILE
PLEASE
DO NOT REMOVE

#9669

14111 Capital Boulevard, Charlotte, NC 28203
Telephone: (704) 554-7913

ATTACHMENT

2

CERTIFICATE OF SERVICE
(UTSE Annual Price Cap Adjustment)

The undersigned hereby certifies that the foregoing Stipulation has been served upon the following counsel of record in Docket No. 96-01423 this 27th day of January, 1997, by FAX, by hand delivery or by placing a copy of the same in the United States Mail postage prepaid and addressed as follows:

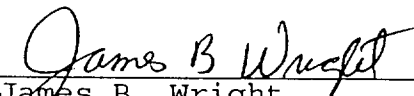
Dianne F. Neal
Tennessee Regulatory Authority
460 James Robertson Parkway
Nashville, TN 37243-0505
FAX 615-741-2336

L. Vincent Williams
Office of the Attorney General
Consumer Advocate Division
426 Fifth Avenue North, 2nd Fl.
Nashville, TN 37243-0500
FAX 615-741-8724

Richard M. Tettelbaum
Citizens Telecommunications Company
of Tennessee, L.L.C.
Suite 500, 1400 16th Street, N.W.
Washington, DC 20036
FAX 202-483-9277

Guy M. Hicks
Bennett L. Ross
BellSouth Telecommunications, Inc.
333 Commerce St., Suite 2101
Nashville, TN 37201-3300
FAX 615-214-7406

John Knox Walkup
Val Sanford (AT&T)
230 Fourth Avenue, North, 3rd Floor
P. O. Box 198888
Nashville, TN 37219-8888
FAX 615-256-6339



James B. Wright

BEFORE THE TENNESSEE REGULATORY AUTHORITY
NASHVILLE, TENNESSEE

IN RE: UNITED TELEPHONE-SOUTHEAST, INC. TARIFF NO. 96-201
TO REFLECT ANNUAL PRICE CAP ADJUSTMENT

DOCKET NO. 96-01423

STIPULATION

This Stipulation is made this 23rd day of January, 1997 by and among United Telephone-Southeast, Inc. ("United"), BellSouth Telecommunications, Inc., Citizens Telecommunications Company of Tennessee, L.L.C., Office of the Attorney General, Consumer Advocate Division, and AT&T of the South Central States, Inc. (herein called the "Parties").

RECITALS

Each of the Parties is a party of record in Docket No. 96-01423 (the "Case") which is pending before the Tennessee Regulatory Authority ("Authority"), and together the Parties constitute all the parties of record in the case.

United is operating under a price regulation plan approved by the Tennessee Public Service Commission effective October 15, 1995.

The Parties have agreed to only those aspects of the methodology expressly stated herein to be used by United in determining its maximum price adjustments under T.C.A. Section 65-5-209(e) (the "Act"), and wish to set forth this agreement in writing.

JBW

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NOW THEREFORE the Parties set forth their Agreement as follows:

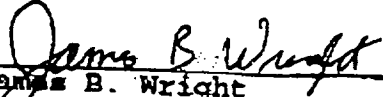
1. The Parties acknowledge that this Stipulation is subject to and conditioned on approval by the Authority or its designee.

2. The stipulated aspects of the methodology to be applied to United under the Act is set forth on the attached nine page document entitled Price Cap Annual Filing Methodology dated January 23, 1997.

3. This Stipulation applies to the stipulated aspects of the methodology only. Each Party specifically reserves the right to contest any other matter or methodology to which there is not an express agreement, including but not limited to those pertaining to the tariff(s) which are or may be filed in connection with any price adjustments proposed in this proceeding.

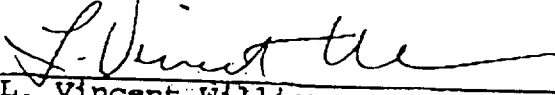
IN WITNESS WHEREOF, the parties have signed this Stipulation effective January 23, 1997.

UNITED TELEPHONE-SOUTHEAST, INC.


James B. Wright
16111 Capital Boulevard
Wake Forest, NC 27587-5900

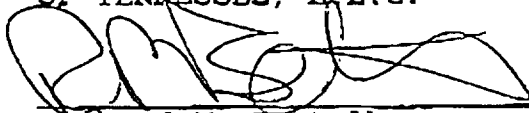
DATED: 1/23/97

OFFICE OF THE ATTORNEY GENERAL
CONSUMER ADVOCATE DIVISION


L. Vincent Williams
426 Fifth Avenue, North, 2nd Floor
Nashville, TN 37243-0500

DATED: 1-24-97

JW

CITIZENS TELECOMMUNICATIONS COMPANY
OF TENNESSEE, L.L.C.

Richard M. Tettelbaum
Suite 500, 1400 16th Street, N.W.
Washington, DC 20036

DATED: 1/24/97

BELLSOUTH TELECOMMUNICATIONS, INC.

Guy M. Hicks
333 Commerce St., Suite 2101
Nashville, TN 37201-3300

DATED: _____

AT&T OF THE SOUTH CENTRAL STATES, INC.
By its Counsel
GULLET, SANFORD, ROBINSON & MARTIN

John Knox Walkup
Val Sanford
230 Fourth Avenue, North, 3rd Floor
Nashville, TN 37219-8888

DATED: _____

#9652

CITIZENS TELECOMMUNICATIONS COMPANY
OF TENNESSEE, L.L.C.

Richard M. Tettelbaum
Suite 500, 1400 16th Street, N.W.
Washington, DC 20036

DATED: _____

BELLSOUTH TELECOMMUNICATIONS, INC.

Guy M. Hicks
333 Commerce St., Suite 2101
Nashville, TN 37201-3300

DATED: 1-24-97

AT&T OF THE SOUTH CENTRAL STATES, INC.
By its Counsel
GULLET, SANFORD, ROBINSON & MARTIN

John Knox Walkup
Val Sanford
230 Fourth Avenue, North, 3rd Floor
Nashville, TN 37219-8888

DATED: _____

00002

GA jaw

CITIZENS TELECOMMUNICATIONS COMPANY
OF TENNESSEE, L.L.C.

Richard M. Tettelbaum
Suite 500, 1400 16th Street, N.W.
Washington, DC 20036

DATED: _____

BELLSOUTH TELECOMMUNICATIONS, INC.

Guy M. Hicks
333 Commerce St., Suite 2101
Nashville, TN 37201-3300

DATED: _____

AT&T OF THE SOUTH CENTRAL STATES, INC.
By its Counsel
GULLET, SANFORD, ROBINSON & MARTIN

John Knox Walkup except as to Item
John Knox Walkup
Val Sanford
230 Fourth Avenue, North, 3rd Floor
Nashville, TN 37219-8888

IV. E. DATED: _____

1/24/97

on page 4

**Price Cap
Annual Filing
Methodology**

January 23, 1997

**United Telephone-Southeast, Inc.
Tennessee**

Table of Contents

I. Purpose

II. Scope

III. Definitions

IV. Methodology

V. Attachments

I. Purpose

On October 15, 1995, United Telephone-Southeast entered Price Regulation per Chapter 408 of the Public Acts of 1995 (the Act) for the state of Tennessee. In response to the Commission's order approving United's plan, the agreement below reflects the stipulated aspects of Price Cap methodology to be used by United in calculating indexes and any price adjustments to ensure compliance with the Act. Other filings implementing aspects of the stipulation may be made throughout the year in response to customer demand, changing market conditions, or to use any residual opportunity for price changes not incorporated into this filing.

II. Scope

As defined by the Act, Basic and Non-Basic Services category revenues and pricing are governed by the Act. A comprehensive list of United's Basic and Non-Basic services, except as noted, is included as Attachment A.

III. Definitions

Below are definitions of terms used throughout this document. A number of the definitions have been presented verbatim from TCA sections, as noted, to support a comprehensive explanation of the calculations.

A. Basic Local Exchange Telephone Services (Basic Services) - are telecommunications services which are comprised of an access line, dial tone, touch-tone and usage provided to the premises for the provision of two way switched voice or data transmission over voice grade facilities of residential customers or business customers within a local calling area, Lifeline, Link-Up Tennessee, 911 Emergency Services and educational discounts existing on the effective date of the price regulation act or other services required by state or federal statute. These services shall, at a minimum, be provided at the same level of quality as is being provided on the effective date of the price regulation act. Rates for these services shall include both recurring and nonrecurring charges. (Section 65-5-208)

B. Non-Basic Services - are telecommunications services which are not defined as Basic Local Exchange Telephone Services and are not exempted under section 65-5-208 (b). Rates for these services shall include both recurring and nonrecurring charges. (Section 65-5-208)

C. Price Regulation Index (PRI) - establishes a ceiling on price changes, in the aggregate, for the Basic and Non-Basic Services categories. The PRI, as of the effective date of Price Regulation, is one hundred (100). The PRI for subsequent years shall be calculated as described in IV.G. below.

D. Service Price Index (SPI) - indicates the cumulative annual percentage change in actual prices, by service category (Basic and Non-Basic), since the effective date of Price



Regulation, or since the last resetting of the Indexes by the Tennessee Regulatory Authority. The SPIs for the Basic and Non-Basic categories are calculated by category and compared to the PRI. The Service Price Index shall be calculated as described in IV.H. below.

E. Gross Domestic Product-Price Index (GDP-PI) - is the final estimate of the Chain-Weighted Gross Domestic Product-Price Index as prepared by the U.S. Department of Commerce and published in the Survey of Current Business, or its successor. (Section 65-4-101 (h)).

F. Revenues per Category - The revenues included in each category are determined as listed below:

Local (Basic and Non-Basic) - revenues are determined from the number of revenue-producing units multiplied by the corresponding per unit price.

Service Connection Charges/Nonrecurring Charges (NRC) - revenues are determined from the number of revenue-producing units multiplied by the corresponding per unit price. To the extent that detailed service volumes can not be specifically linked to a basic service or specifically linked to a non-basic service, the company will propose a method of allocation and provide documentation supporting the allocation to the Tennessee Regulatory Authority and interested parties. Any interested party may petition the Authority for a hearing on the appropriate allocation method. For United's initial filing, the parties stipulate that the Service Connection and NRC charges are properly allocated between Basic and Non-Basic Services based upon the percentage of revenues where charges are applicable for each category.

Message Toll, Switched Access, Opportunity 800, WATS - revenues are derived from minutes of use multiplied by the corresponding per minute price.

Switched Access - Dedicated, Special Access - revenues are derived from the number of units multiplied by the corresponding per unit price.

Billing and Collection, Public and Semi-Public Phone Revenue, Cellular Interconnection, Directory Compensation, Miscellaneous - revenues are determined from the number of revenue-producing units multiplied by the corresponding per unit price. To the extent that detailed service volumes are not available for any such service, the Company will propose a method for determining these revenues and provide documentation supporting its calculations to the Tennessee Regulatory Authority and interested parties. Any interested party may petition the Authority for a hearing on the proposed method for determining these revenues.

JBW

G. Revenue Producing Units - The units included in the service volumes are revenue-producing units only. Company official units are excluded from the service volumes.

IV. Methodology

A. Increases in the Basic Local Exchange category - cannot occur until October 15, 1999.

B. Call Waiting - Rates for call waiting have been set at \$3.00 for residence customers and \$3.90 for business customers until October 15, 1999 per the Act.

C. Interconnection Services - Prices for interconnection services are capped at the lesser of one-half (1/2) the percentage change in the previous year's inflation rate or the inflation rate for the previous year minus two percentage points (TCA 65-5-208). The inflation rate is defined as the percentage change in the final estimate of the Chain-Weighted GDP-PI from the most recent quarter when a final estimate is available. For this filing, the 1996 first quarter inflation rate is used. Subsequent evaluations for United Telephone-Southeast, Inc. will continue to use first quarter estimated inflation rates. Interconnection includes the ability for telecommunications carriers, including Competitive Local Exchange Companies, Cellular service providers, Wireless service providers, etc., to interconnect directly or indirectly with the facilities and equipment of other telecommunications carriers and obtain access to network elements on a non-discriminatory basis dependent on the cost of providing the network element (per the Telecommunications Act of 1996, Section 251, Interconnection).

D. New Services - New tariffed services will be included in the SPI for the appropriate category in the first annual filing after the service has been available for six months. The price in effect for the new service when it is added to the index calculations, divided by the value of the Service Price Index for the previous anniversary date, shall be the initial index price for the new service.

E. Revenue Neutral Filings - Revenue neutral filings are defined as filings that result in no increase in aggregate revenues. Revenue neutral filings will not include SPI calculations when services within the same category are affected.

F. Promotional Pricing - The permanent approved rates shall be used in calculating revenues for services where rates are discounted for promotional purposes during the year.

G. Calculation of PRI - Per the Act, the "maximum annual adjustment...is capped at the lesser of one-half (1/2) the percentage change in inflation for the United States using the

JBW-1

Gross Domestic Product-Price Index (GDP-PI) from the preceding year as the measure of inflation, or the GDP-PI from the preceding year minus two (2) percentage points" (TCA 65-5-208). The Price Regulation Index is calculated annually as a) 100 plus b) the lesser of one-half (1/2) the percentage change in the previous year's inflation rate or the inflation rate for the previous year minus two percentage points c) divided by 100 and d) multiplied by the then current value of the PRI for the company. The inflation rate is defined as the percentage change in the final estimate of the Chain-Weighted GDP-PI from the most recent quarter when a final estimate is available. Attachment B reflects the calculation. Future years will use appropriately updated inflation rates.

H. Calculation of SPI for Basic and Non-Basic Services - The Service Price Index is calculated for both Basic and Non-Basic categories as 1) the annualized Proposed revenues for each category 2) divided by the annualized Base revenues for each category 3) multiplied by 100. The annualized Proposed revenues for each annual filing shall be the revenues for each category resulting from pricing out the annualized service volumes for the latest month available at the company's current prices for each service plus the net effect of any proposed price changes. The service volumes for the latest month available are for the month of June for the year of the annual filing. The annualized Base revenues for each annual filing shall be the revenues resulting from pricing out the annualized service volumes for the latest month available at the company's initial index prices for each service. The initial index prices are the service prices in effect on June 6, 1995 or as reset by the Tennessee Regulatory Authority under TCA 65-5-207. If the PRI and SPI are reset by the Authority, the same proportional relationship will exist between these two indexes before and after the resetting process. The SPI will be recalculated with each annual filing and as necessary for interim filings. The service volumes will remain constant for interim filings and will be adjusted with each annual filing.

V. Attachments

A. List of Basic and Non-Basic Services as of 6/30/96

B. 1996 PRI Calculation

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Attachment A

List of Basic and Non-Basic Services as of 6/30/96

Basic Services	Tariff	Section	Revenue Category
ABC Network Access Registers (NARS) (plus one line per NAR)	GSST	13.18.7 B	Local
Exchange Access and Usage (including Key/PBX trunks)	GSST	3	Local and Measured
In-classroom Computer Access	GSST	3.12.3	Local
Lifeline Service	GSST	3.10.3	Local
Link-up Tennessee	GSST	4.11	Local
Shared Tenant Service	GSST	3	Local
Touch Tone	GSST	13.7.2	Local
* Other Services required by State and Federal Statutes			
Non-Basic Services	Tariff	Section	Revenue Category
ABC Intercom Lines & Features (less one line per NAR)	GSST	13.18.7	Local
ABC Medical Community	GSST	13.18.8	Local
Analog Private Lines	GSST	22.2.1	Local
Billing and Collection	Access	8	Billing and Collection
Coin Telephone Service - Pub and Joint Oper	GSST	7	Public and Semi-Public Phone
Custom Calling Services and Packages	GSST	13.9	Local
DID Service	GSST	13.14.2	Local
Directory Assistance	Not in tariff		Local
Directory Compensation	Contract		Directory Compensation
Directory Listings (Foreign, Add'l, etc)	GSST	6	Local
E-911	GSST	21	Local
Enterprise Service (Special Reverse Toll)	GSST	13.8	Local
ExpressTouch Services	GSST	13.20	Local
Extension Service	GSST	13.1	Local
Frame Relay Service	New Service		Local
FX Service	GSST	9.1.2	Local
Interconnection of Mobile Service	GSST	16.10	Cellular Interconnections
ISDN BRI and PRI	GSST	12	Local
Maintenance of Service Charge	GSST	15.4	Local
MessageLine	GSST	13.24	Local
MTS	MTS		Message Toll
Miscellaneous	Contract		Miscellaneous
N11 Service	GSST	10	Local
Operator Service	GSST	3.18	Local
Optional Calling Plans	GSST	20	Local
PBX Night, Sunday, etc. Arrangements	GSST	11.3.2	Local
Public Announcement Service	GSST	13.12	Local
Restriction Services	GSST	13.17	Local
Station Message Desk Interface (SMDI)	GSST	13.22	Local
Switched and Special Access	Access	6,7	Switched Access-Ded Switched Access Special Access
Telecommunications Service Priority System	GSST	13.21	Local
Telephone Answering Service	GSST	8.2	Local
Tie Service	GSST	13.3	Local
United DigiLink/Translink	GSST	22.4 & 22.5	Local
United Flexlink	GSST	22.6	Local
United Lightlink	GSST	22.7	Local
United Switchlink	GSST	13.23	Local
WATS	GSST	19.4	Local, WATS, Opportunity 800

* Categorization as Basic or Non-Basic is an issue to be determined in this proceeding.

1996 PRI Calculation

Input:

Inflation Rate 2.4
First Qtr 1995 vs. First Qtr 1996

Calculation:

Step 1:
Base Rate of 100 100

Step 2:
Plus: The lessor of:

1/2 Inflation Rate 1.2

or

Inflation Rate - 2% 0.4

= 100.4

Step 3:
Divided by 100 1.004

Step 4:
Multiplied by the current PRI (100) 100.4



SURVEY OF CURRENT BUSINESS

8. Supplementary Tables.

Table 8.1.—Percent Change From Preceding Period in Selected Series
[Percent]

	Seasonally adjusted at annual rates								Seasonally adjusted at annual rates										
	1994	1995	1994						1995	1994	1995	1994						1995	1996
			IV	I	II	III	IV	I				IV	I	II	III	IV	I		
Gross domestic product:																			
Current dollars	5.8	4.5	6.4	3.9	2.8	5.8	2.3	4.3											
Chain-type quantity index	3.5	2.0	3.2	.6	.5	3.6	.5	2.2											
Chain-type price index	2.3	2.5	2.2	3.3	2.5	2.2	2.2	2.4											
Implicit price deflator	2.3	2.4	2.2	3.2	2.3	2.2	1.8	2.1											
Personal consumption expenditures:																			
Current dollars	5.5	4.8	5.3	3.4	4.1	4.2	2.6	5.8											
Chain-type quantity index	3.0	2.4	3.3	.8	3.4	2.8	1.2	3.6											
Chain-type price index	2.4	2.4	2.0	2.7	2.8	1.5	1.7	2.4											
Implicit price deflator	2.4	2.3	2.0	2.6	2.7	1.4	1.4	2.1											
Durable goods:																			
Current dollars	9.5	4.4	12.4	-6.2	7.6	8.1	-2.0	5.4											
Chain-type quantity index	7.2	3.4	12.6	-8.7	7.0	9.3	.3	8.5											
Chain-type price index	2.1	1.4	-1	3.1	.8	-7	-2	1.2											
Implicit price deflator	2.1	1.0	-2	2.7	.5	-1.2	-2.3	-1											
Nondurable goods:																			
Current dollars	4.4	3.9	4.4	3.5	4.2	1.2	.9	7.7											
Chain-type quantity index	3.1	2.3	3.2	2.4	1.9	.5	-3	3.6											
Chain-type price index	1.3	1.7	1.2	1.0	2.6	.7	1.3	3.9											
Implicit price deflator	1.3	1.8	1.1	1.1	2.3	.7	1.3	3.9											
Services:																			
Current dollars	6.2	5.3	4.3	5.6	6.8	5.0	4.6	4.2											
Chain-type quantity index	2.1	2.3	1.4	2.1	3.4	2.5	2.2	2.5											
Chain-type price index	3.0	3.1	2.8	3.6	3.4	2.4	2.4	1.9											
Implicit price deflator	3.0	3.0	2.9	3.4	3.3	2.4	2.3	1.7											
Gross private domestic investment:																			
Current dollars	10.6	5.0	6.8	8.8	-7.9	9.7	-4.0	1.0											
Chain-type quantity index	14.3	3.2	5.0	7.3	-9.7	7.4	-3.7	3.0											
Chain-type price index	1.9	1.9	1.4	1.0	3.0	2.3	.8	.4											
Implicit price deflator	1.9	1.7	1.5	1.2	2.1	2.1	-3	-1.0											
Fixed investment:																			
Current dollars	12.3	7.7	9.8	9.4	.9	8.2	3.7	9.7											
Chain-type quantity index	10.1	6.1	6.4	6.8	-1.4	8.3	4.0	11.3											
Chain-type price index	1.9	1.8	1.2	.8	2.7	2.3	.7	.9											
Implicit price deflator	1.8	1.5	1.2	.7	2.4	1.8	-3	-1.2											
Nonresidential:																			
Current dollars	11.4	10.7	12.0	15.5	6.1	6.8	1.8	10.7											
Chain-type quantity index	9.8	9.6	12.2	15.3	3.8	5.2	3.1	12.4											
Chain-type price index	1.4	1.2	-1	.1	2.8	2.0	.1	.1											
Implicit price deflator	1.4	.9	-2	.2	2.5	1.3	-1.3	-1.5											
Structures:																			
Current dollars	4.8	10.8	18.5	12.8	6.5	10.3	2.9	9.0											
Chain-type quantity index	1.6	7.2	13.0	9.9	3.4	8.2	.9	7.9											
Chain-type price index	3.3	3.3	4.9	2.4	2.9	3.8	1.8	1.3											
Implicit price deflator	3.3	3.3	4.8	2.6	3.1	3.8	2.0	1.0											
Producers' durable equipment:																			
Current dollars	14.1	10.6	9.7	16.6	6.0	5.3	1.4	11.3											
Chain-type quantity index	13.2	10.5	11.9	17.4	3.7	4.8	4.0	14.1											
Chain-type price index	.7	.4	-1.8	-7	2.7	1.4	-5	.4											
Implicit price deflator	.7	.1	-2.0	-7	2.3	.4	-2.4	-2.4											
Residential:																			
Current dollars	14.3	.7	4.4	-4.2	-11.1	12.5	8.8	7.3											
Chain-type quantity index	10.8	-2.3	-1	-6.3	-13.5	9.2	6.4	7.4											
Chain-type price index	3.1	3.1	4.6	2.2	2.8	2.9	2.2	-1											
Implicit price deflator	3.1	3.1	4.5	2.2	2.5	3.0	2.2	-1											
Exports of goods and services:																			
Current dollars	8.4	11.4	17.0	6.1	9.7	8.1	8.8	1.1											
Chain-type quantity index	8.3	8.3	15.3	2.6	4.6	8.0	11.0	2.0											
Chain-type price index	1.1	3.3	2.2	5.8	5.3	.9	.8	.4											
Implicit price deflator	1.1	2.9	1.5	5.4	4.8	.1	-2.0	-9											
Exports of goods:																			
Current dollars	10.8	14.2	23.0	10.3	11.9	9.5	10.6	-5											
Chain-type quantity index	10.1	10.8	21.3	3.7	6.8	9.6	14.1	2.1											
Chain-type price index	.6	3.6	2.9	6.9	5.3	.9	-1.6	-9											
Implicit price deflator	.6	3.0	1.9	6.3	4.8	0	-3.1	-2.6											
Exports of services:																			
Current dollars	8.2	4.9	2.4	2.7	4.7	4.3	4.5	5.6											
Chain-type quantity index	4.0	2.3	1.8	-3	-4	3.9	3.4	1.9											
Chain-type price index	2.1	2.6	.9	3.1	5.2	.4	1.1	3.6											
Imports of services:																			
Current dollars	5.8	4.8	-8	7.0	10.1	0	4.5	11											
Chain-type quantity index	5.2	2.0	-4.8	11.6	-3.5	1.5	8.8	12											
Chain-type price index	1.5	2.8	3.9	-4.1	14.8	-1.4	-1.9	-1											
Implicit price deflator	1.5	2.7	4.0	-4.1	14.1	-1.4	-1.7	-1											
Government consumption expenditures and gross investment:																			
Current dollars	1.9	3.3	1.7	3.8	4.2	1.4	-3	6											
Chain-type quantity index	0	.1	-1.4	-1.1	.9	-7	-4.1	1											
Chain-type price index	2.0	3.4	3.2	5.1	3.3	2.1	4.4	4											
Implicit price deflator	2.0	3.3	3.1	5.0	3.3	2.0	4.0	4											
Federal:																			
Current dollars	-1.1	.1	-2.1	-8	2.1	-4	-6.8	8											
Chain-type quantity index	-3.7	-3.5	-5.9	-6.3	-1.1	-5.9	-12.8	5											
Chain-type price index	2.7	3.8	4.2	6.2	3.2	1.7	7.6	1.5											
Implicit price deflator	2.7	3.7	4.0	5.9	3.3	1.6	7.0	2.6											
National defense:																			
Current dollars	-2.8	-1.8	-13.1	-2.2	6.3	-7.3	-0.5	8.2											
Chain-type quantity index	-5.1	-5.0	-16.1	-7.0	.9	-8.1	-12.0	3.8											
Chain-type price index	2.4	3.7	3.8	5.6	4.4	1.0	3.5	2.5											
Implicit price deflator	2.4	3.4	3.5	5.2	4.4	.8	2.8	4.2											
Nondefense:																			
Current dollars	2.9	4.1	26.3	2.1	-4.2	1.9	-1.2	10.1											
Chain-type quantity index	-7	-2	20.2	-4.8	-6.2	-1.2	-14.6	10.1											
Chain-type price index	3.5	4.4	5.1	7.5	.7	3.2	17.0	.4											
Implicit price deflator	3.6	4.3	6.1	7.3	1.1	3.2	15.7	0											
State and local:																			
Current dollars	4.0	5.4	4.2	6.8	5.5	3.1	3.8	4.5											
Chain-type quantity index	2.5	2.4	1.6	2.3	2.1	2.7	1.5	-9											
Chain-type price index	1.5	3.0	2.5	4.4	3.3	2.3	2.3	5.5											
Implicit price deflator	1.5	3.0	2.5	4.4	3.3	2.3	2.3	5.4											
Addenda:																			
Final sales of domestic product:																			
Current dollars	5.2	4.0	6.8	4.0	4.2	5.6	3.6	5.4											
Chain-type quantity index	2.9	2.4	3.6	.7	1.8	3.4	1.6	3.3											
Chain-type price index	2.3	2.6	2.2	3.3	2.4	2.2	2.2	2.4											
Implicit price deflator	2.3	2.4	2.1	3.2	2.3	2.1	1.8	2.1											
Gross domestic purchases:																			
Current dollars	8.2	4.6	4.8	4.2	3.8	4.6	1.1	6.3											
Chain-type quantity index	3.9	2.1	2.7	1.4	.9	2.8	-5	3.1											

Percentage change in
final estimate of
Chain-Weighted GDP-PI

NOTE—Except for deductible personal income, the quantity and price indexes are calculated from complete surveys of the detailed output and prices used to prepare each aggregate and component. Prior to the third quarter of 1964, these indexes use the geometric mean of weights that reflect the composition of output for the preceding and current years. Beginning with the third quarter of 1964, these indexes use weights that reflect the composition

of meat in the impact price indexes are weighted averages of the detailed price indexes and is prepared with explicit and consistent and are calculated on the basis of current to chain-linked output weighted by 100 (Contributions to the percent change in real gross domestic product are shown in table 5.7)